

Exhibit No. 1

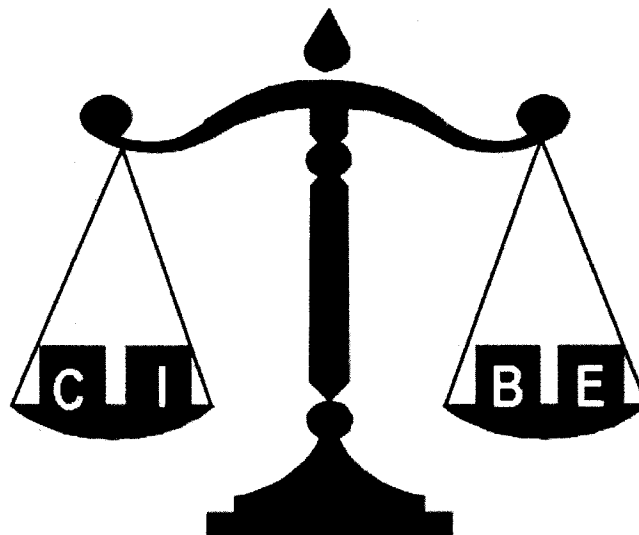
Date 1-15-07

Bill No. Informational Meeting

# MONTANA TEACHERS' RETIREMENT SYSTEM

## State Administration Committee

2007 Legislative Session



C = Contributions

B = Benefits

I = Investment Income

E = Expenses

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# **MONTANA TEACHERS' RETIREMENT SYSTEM**

## **THE TEACHERS' RETIREMENT BOARD**

- Governed by a six-member Board appointed by the Governor
- Four members are appointed from the teaching profession
  - One must be an active classroom teacher
  - One a retired member
- Two members are appointed as representatives of the public
- The Board is responsible for the administration of the system and hires a staff of 17 to carry out these duties on a daily basis. The Board Of Investments (BOI) is responsible for investing the assets of the Teachers' Retirement System

### **Board Members**

### **Term Expires**

TIM RYAN - Public Member  
Big Fork, MT

July 1, 2009

SCOTT DUBBS - Active Member  
Lewistown, MT  
Chair

July 1, 2008

KARI PEIFFER - Active Classroom Teacher  
Kalispell, MT  
Vice Chair

July 1, 2007

DARRELL LAYMAN - Retired Member  
Glendive, MT

July 1, 2011

MONA BILDEN - Active Member  
Miles City, MT

July 1, 2011

JAMES TURCOTTE - Public Member  
Helena, MT  
(Also a member of BOI)

July 1, 2010

## **OVERVIEW OF THE TEACHERS' RETIREMENT SYSTEM**

- Established by the Legislature effective July 1, 1937
- Initial membership of 3,367, to over 18,000 active members
- Over 11,000 retired members or their beneficiaries
  - Currently receiving benefits of approximately \$171 million per year
- Assets of over \$2.7 billion as of July 1, 2006
- Unfunded Liabilities as of July 1, 2006 were over \$863.1 million

The TRS Summary of Information handbook and the 2006 Annual Report are available at: <http://www.trs.mt.gov/publications/Publications.htm>

### **Summary of TRS Benefit Provisions**

Vesting Period	5 years. No benefits are payable unless the member has a vested right, except the return of employee contributions with interest.
Benefit Formula	Total years of service times Average Final Compensation (AFC) times 1.666667% = Annual Benefit
Average Final Compensation	Average of highest 3 consecutive years of earned compensation.
Normal Form of Benefits	Life only annuity. All benefits cease upon death; however, in no event will the member receive less than the amount of employee contributions with interest.
Normal Retirement Benefits	Minimum of 25 years of service at any age, or age 60 with at least 5 years of service.
Early Retirement Benefits	At least 5 years of service and age 50.
Benefit:	The retirement benefit is calculated in the same manner as described above, but the benefit is reduced 1/2 of 1% for each of the first 60 months early and 3/10 of 1% for each of the next 60 months early.
Survivors Benefit	
Eligibility:	Member must have had at least 5 years of service.

Benefit:	The death benefit is equal to Normal Form benefit accrued at date of death, with an actuarial adjustment based on the relation of the member's age at death to the beneficiary's age. A monthly benefit of \$200 is paid to each child until age 18. In addition, a lump-sum benefit of \$500 is paid upon the death of an active or retired member.
Disability Benefit	
Eligibility:	Member must have had at least 5 years of service, and totally disabled for the further performance of your duties.
Benefit:	The disability benefit is equal to 1/60 of AFC for each year of service accrued at date of disability. The minimum benefit is 1/4 of the AFC.
Withdrawal Benefits	With less than 5 years of service, upon termination, the accumulated employee contributions with interest are returned. With more than 5 years, the member may elect a refund of contributions with interest or leave the contributions and interest in the System and retain a vested right to future retirement benefits.
Contributions	<p>Member: 7.15% of compensation.  Employer: 7.47% of compensation.  State: 0.11%</p> <p>MCA 19-20-604 specifies that the State's contribution rate will cease when the amortization period of the System's unfunded actuarial liability is 10 years or less according to the System's latest actuarial valuation.</p>
Interest on Member Contributions	Interest on member contributions is currently being credited at a rate of 4.0% per annum.
Guaranteed Annual Benefit Adjustment	On January 1 of each year, the retirement allowance payable must be increased by 1.5% if the retiree's most recent retirement effective date is at least 36 months prior to January 1 of the year in which the adjustment is to be made.

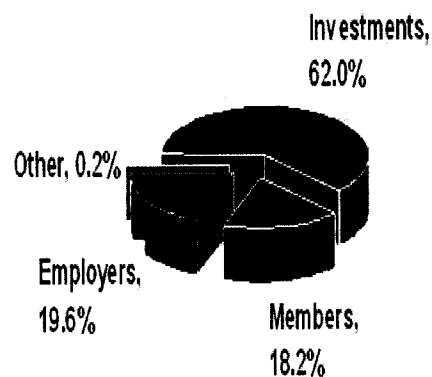
# Source Of Funding

- Based on 2005-06 cash flows - investment returns:

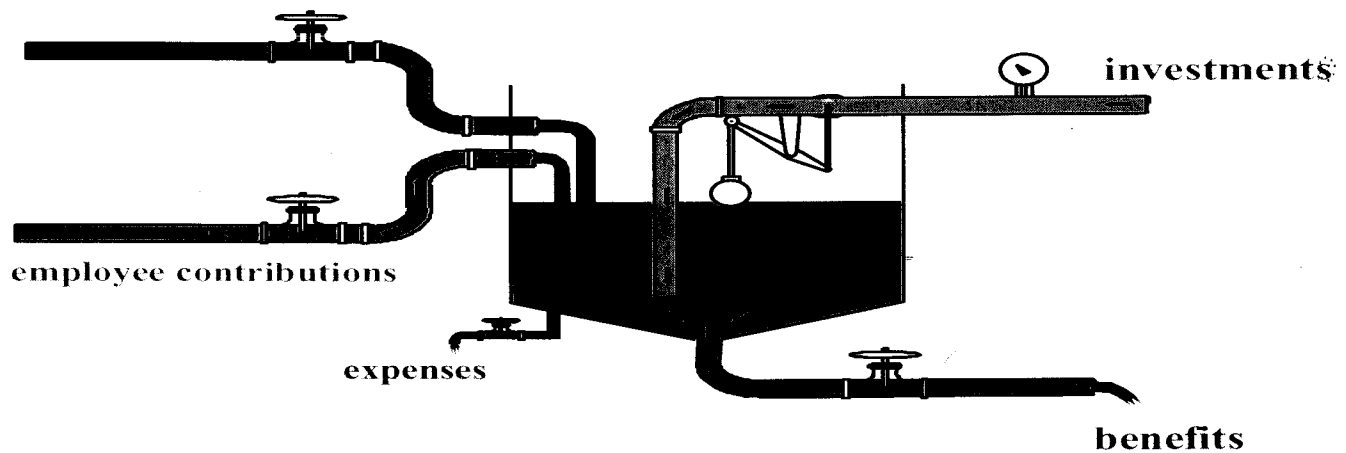
(Minimum) 7.75%

- Employee Contribution  
7.15%
- Employer Contribution  
7.47%
- State Contribution  
0.11%

TRS Funding Sources



## FUNDING PRINCIPLE



### Historical Returns\*

<i>Fiscal Year Ending</i>	<i>Market Returns</i>	<i>Amortization Period</i>
<i>June 30, 1998</i>	16.6%	9.20
<i>June 30, 1999</i>	11.9%	
<i>June 30, 2000</i>	7.8%	15.10
<i>June 30, 2001</i>	(5.1)%	
<i>June 30, 2002</i>	(7.3)%	23.4
<i>June 30, 2003</i>	6.2%	
<i>June 30, 2004</i>	13.3%	> 30.0 years
<i>June 30, 2005</i>	8.0	> 30.0 years
<i>June 30, 2006</i>	8.9	> 30.0 years

\* Effective July 1, 2004 the actuarial investment rate of return is assumed to be 7.75% per year, compounded annually. Anything less is a loss, and will eventually increase the amortization period if not offset by future gains, contribution increase, or reduction in benefits.

## **FUNDING RETIREMENT BENEFITS**

The Montana Constitution, Article VIII, Section 15, requires that all public retirement systems be funded on an actuarially sound basis. The acceptable period of time to fund the Unfunded Actuarial Accrued Liability (UAAL), as established by the Governmental Accounting Standards Board (GASB), is 30 years.

- What is the UAAL and what does it mean to the TRS members?
  - It is a gap between the promised benefits and the amounts that will be available to pay those benefits. It represents an outstanding obligation of the State to the plan and its members.
- As of July 1, 2006, the TRS UAAL was over \$863.1 million.
- Currently the State and all TRS employers make regular payments toward the UAAL every month. The problem is that current rates are not sufficient to amortize the UAAL over any period of time.
  - State            0.11%
  - Employers    4.25%
- Whenever the TRS' investment earnings exceed the actuarial assumed rate, currently 7.75%, the additional income reduces the UAAL.

**Funding Concerns** - The following examples all impact the actuarial funding of TRS either because benefits (liabilities) are increased for which no additional funding is received, or because benefits start before the member actually terminates employment and truly retires, or benefits simply begin earlier than anticipated.

- **End Of Career Pay Raises** - Percentage or flat dollar increases are granted in the last 2 or 3 years of employment and in return, the TRS member gives notice they will retire. Montana's statutes are clear that these kinds of raises are not reportable to TRS; however, to the extent these practices get past us, they contribute to the unfunded problems of the system.
- **Bona Fide Separation From Service** - Without a true termination and a break in service, the TRS is in danger of violating IRS restriction on in-service distributions. In addition, members who are rehired without any break in service raise questions regarding termination and eligibility for benefits. During any school year 500 – 600 retirees are reported to TRS as having returned to work in a part-time position, most only for a few days, but a few work the entire year in positions paying the maximum they can earn under TRS rules plus additional fringe benefits excluded from the definition of earned compensation under §19-20-101(6), MCA. Resulting in benefits being paid before a member actually terminates and retires thus increasing the unfunded liabilities of TRS.

- Benefit Swaps for Additional Salary – Adding salary to the contract in lieu of employer paid benefits for the purpose of enhancing a member's benefit is at the very least unethical and probably illegal. The TRS statutes clearly state that if an employer converts employer paid benefits, e.g. insurance or housing, to cash compensation that they must: one, do so for all employees, and converted benefits must be reported to the TRS for at least 5 years before the additional earnings can be used in the calculation of average final compensation.

### **Funding Options – 2007 Legislation (HB 63)**

- Infusion of cash
- Increase State's General Fund Contribution
- Reducing liabilities through closing loopholes and clarifying current statutes discussed above will certainly help reduce the need to increase contribution rates.

### **New Plan Design – New Members Only**

One of the purposes of a retirement plan is to attract and retain quality workers. As the baby boomers begin to exit the system and enter the next phase of their life it is time to also reflect on the current benefits provided by the TRS and ask if this is going to be the right plan design for members entering the System today when they get ready to retire 25, 30, or 40 years from now. In other words, will the current system meet the needs of future retirees?

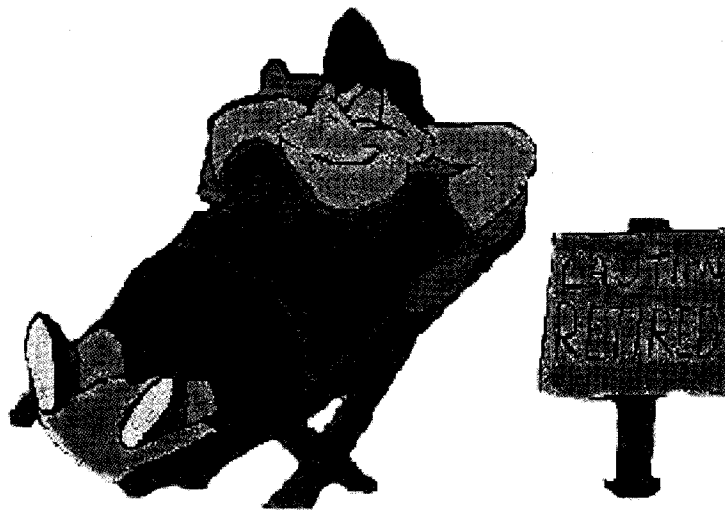
Unfortunately, our retirement systems are still largely based on an era when life expectancy was much lower. In addition, the nature of work and compensation has also changed so as to encourage earlier retirement than we can afford.

### **Alternative plan designs for new members currently being discussed include:**

- The current design but with diminished benefits
- Defined Contribution 401(K) type plans
- Age Based Plans requiring a minimum age and number of years of service
- Money Purchase Plans where benefits are based on the members age at retirement regardless of the number of years of service. The longer you work the larger the benefit.



**ANY QUESTIONS?**



**TEACHERS' RETIREMENT SYSTEM**